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SUBJECT: MOLSS Mulls Management of 31 Billion RMB in Rural Pension Assets

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¶1. (U) Summary: China's Ministry of Labor and Social Security (MOLSS) is working to establish a pension system for rural and migrant workers that will require low contributions, be portable and have broad coverage, according to the Deputy Director General (DDG) of the Ministry's Rural Pensions Division. Migrants with stable jobs have the right to participate in the urban pension system with contribution rates of 28 percent and comparatively high benefits. However, to provide pensions for rural residents and those migrants who travel from place to place, the rural pension system will require an enterprise contribution of 10 percent of the worker's salary, of which 6 percent will be placed in the rural or migrant worker's individual account, plus a worker contribution of 5 percent of salary, all of which will go into the individual account. Portability is difficult to achieve because urban system "legacy" pensions, those owed workers under the planned economy, easily deplete the pooled accounts from which current pension benefits are paid, necessitating "borrowing" from the individual accounts; information technology could help solve the problem by tracking both "borrowed" funds and individual accounts as people move from place to place. Rural pension funds, which currently total 31 billion rmb (At mid-May exchange rate of RMB 8:USD 1, rural pension funds amount to approximately USD 3.9 billion) in assets (Note: In a related document, reference was made to 70 billion rmb (USD 8.75 billion) in assets. End Note.), are managed at the county level. There is recognition that pension funds must earn a higher rate of return. MOLSS officials hope to travel to the United States to better understand how the United States manages pension funds. If travel does not occur, Laboff will again propose to MOLSS that the Embassy arrange a digital video conference to allow Washington agencies and interested others to address some of MOLSS' questions. End Summary.

¶2. (U) Econoff met with Liu Conglong, Deputy Director General, Rural Pension Division, Ministry of Labor and Social Security (MOLSS) on May 17 regarding China's progress toward establishing a rural social security system. DG Liu noted that his work had been given support and impetus by the Government's 2006 Document Number 1 setting out guidelines for building the new countryside. The National People's Congress included the development of a rural pension system, on which MOLSS is working with the Ministry of Finance, in the 11th Five Year Plan. The Number 5 document issued by the Government also called for solving the problem of migrant workers.

¶3. (U) The Government's Number 29 document, according to DDG Liu, requires the establishment of a social security system and an occupational training system for farmers whose land has been taken for development. MOLSS must issue the guidelines for this program within one year, DDG Liu said. To prepare for these programs, MOLSS has calculated that there are currently 200 million farmers who have left farming to become workers. Of these, 130 million farmers-turned-workers work in township and village enterprises (TVEs) near their place of residence. An additional 70 million migrants migrate back and forth from the cities. (Note: There is probably overlap between these two figures, as some migrants move back and forth between rural areas to work. However, the number cited for migrants in the cities differs from other estimates Embassy has seen. MOLSS, based on an April 2004 survey, has published estimates that there are approximately 100 million rural migrants currently working in cities. The National Bureau of Statistics, based upon results of a 2004 sample survey, estimated that there were approximately 120 million rural migrants working in the cities. The Ministry of Agriculture, in an undated study, concluded that approximately 130-140 million migrant workers and their

family members work and reside in the cities. End Note.) There is a rural social security office established in MOLSS. In addition, a State Council Joint Coordinating Committee on migrant workers, headed by Secretary General Hua Jianmin has been established.

¶4. (U) DDG Liu described the social safety net of programs that has been established, and in which enrollment is being expanded, to protect migrant workers:

-- Workers' Compensation: Employers are required by a 2004 regulation to enroll all migrant worker employees in the workers' compensation insurance program. MOLSS is especially targeting construction and mining industries where many migrants work.

-- Medical Insurance: A medical insurance program for migrants has also been mandated. This program is intended to insure migrants against the costs of 1) major illnesses, 2) hospitalization; and 3) illnesses and injuries for which immediate treatment is needed. (Note: A May 19 article in the China Labor and Social Security News reported that the Shanxi provincial government had established such a medical insurance system for migrants. The article stated that all employers must pay 3 percent of the insured's wage to the local Labor and Social Security Bureau, out of which 3 percent, 2.5 percent goes into a pooled account for basic medical insurance, and the remaining 0.5 percent goes into a pooled account for catastrophic expenditures. According to the article, migrants with long-term, stable working relationships may enroll in the urban medical insurance system. End Note.)

Rural Pensions: Portable, Low Contributions, Wide Coverage
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¶5. (U) DDG Liu said that a system of pensions for rural and migrant workers in China must have three characteristics:

-- Portability: Pensions should be portable, benefiting individual participants and the system as well, DDG Liu said. Currently, the few pension systems in which migrants and rural

residents can participate are not portable. As a result, migrants do not want to pay into the system because when the migrant changes jobs, he cannot take his pension contributions or the contributions of the employer, with him. (Note: The contributions remain in the local system, while the migrant moves on, never meeting vesting requirements in any given place, and never receiving a pension benefit. End Note.) Currently, some local systems may allow portability within a restricted area, but the individual must remain within that area in order to receive benefits. Finally, most systems require that the migrant or rural worker pay into the system for 15 years before gaining the right to receive a pension upon retirement. Few migrants remain that long in any given place, DDG Liu said.

-- Low Contributions: Migrant contributions should be low because migrant workers are systematically underpaid. This is the case, DDG Liu said, because current minimum wage regulations state that the minimum wage should be set at a percentage of the average local salary. However, he said, that is not the case.

-- Wide Coverage: As many rural and migrant workers as possible should be included in the system.

Stable Employment Allows Participation in Urban Pension System
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¶6. (U) For analytical purposes, MOLSS has divided farmer workers into two types: 1) those with stable employment, and 2) those whose employment is not stable. The first group should be treated like urban workers, and given the right to participate in the urban pensin system, DDG Liu said. However,

the urban system requires that workers contribute to the system for 15 years before having the right to draw a pension at retirement. This is a problem that must be solved for migrant workers, whose work life often does not span a full 15 years. To accommodate the frequent changes of employment experienced by migrants who do not have stable employment, MOLSS has decided that contributions by both the employer and the employee will go into the individual account, and that the individual account will be portable.

¶7. (U) The urban pension system is not suited to the needs of migrants and farmers because the urban pension system has been burdened with the cost of "legacy" pensions, pensions for individuals who were entitled to pensions under the old planned economy. In order to be able to afford to pay those legacy pensions, the newly established urban pension system levied high contribution rates for current participants. (Note: Contribution rates are approximately 28 percent of wages; 20 percent is deposited into the pooled account from which current pensions are paid, and 8 percent, the employee's contribution, is paid into the individual account. End Note.) Migrants and farmers who do not have stable employment are unable to contribute at these rates, DDG Liu said. However, if a migrant has stable employment, he may decide he wants to participate in the urban system. In Shanxi, for example, an enterprise might have urban workers and migrant workers with stable employment, both of whom can participate in the urban system, as well as local farmers or migrant workers who can elect to participate in the rural pension plan, and to have their contributions made into their individual account.

Rural System: 11 Percent of Salary to Individual Account
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¶8. (U) MOLSS has decided that the appropriate contribution rate for the rural pension system should be from 5 to 10 percent of salary. The enterprise contributes 10 percent of salary, of which 6 percent is placed in the rural or migrant worker's individual account. The worker himself pays a contribution of 5 percent of salary, all of which goes into his individual account. Therefore, a total of 11 out of 15 percent is paid into the worker's individual account. The remaining 4

percent of the employer's contribution is retained in a fund from which "adjustments" can be made.

Rural Pensions Pooled and Administered at the County Level

¶9. (SBU) Currently, there are 1,900 county level units participating in the rural system of pensions, which covers 54 million persons. Of this 54 million persons, 420,000 are farmers and the other approximately 53.5 million persons are migrant workers. The total accumulation of pension funds has reached 31 billion rmb. (USD 3.9 billion) (Note: In a paper describing a hoped-for delegation to the United States by the Department of Rural Social Insurance, the total value of assets of the Chinese rural social insurance system was described as 70 billion rmb. (USD 8.75 billion) End Note.)

¶10. (U) County governments, which manage the rural pension funds, have been asked to make contributions to the system, and have complied by paying in. (Note: Although DDG Liu did not so specify, these contributions are likely contributions in lieu of an employer's contributions for farmers who continue to farm and who are not otherwise employed. End Note.) In Beijing, the municipal government has contributed 15 million rmb to enroll migrant workers in the system, thus encouraging participation. In the Daxing District of Beijing, the District pays 15 million rmb (USD 1.8 million) every year for the participation of 50,000 farmers; the district's pension system has a total of 230,000 farmers enrolled.

"Legacy" Pensions Make Establishing a Portable System Difficult

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¶11. (U) Establishing a portable system is difficult, DDG Liu said, because the problem of urban pensions has not yet been solved. Even with high contribution rates, the urban system's pooled accounts have not accumulated sufficient funds to pay current pensions; as a result, the localities have "borrowed" from the individual accounts. As a result, the individual accounts in many if not most parts of the urban system are unfunded. One way to resolve this problem is to have a nationwide information technology (IT) system for the social security system to keep track of amounts "borrowed" as well as to track individual accounts as people move from place to place.

Pension System Needs Investments Yielding High Rate of Return
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¶12. (U) There is also recognition, DDG Liu said, that the system must ultimately allow for investments that will make the funds increase in value. A 1999 regulation says that social security funds should be invested in bank accounts and bonds. However, MOLSS is actively seeking a safe way to invest in key projects that provide a higher rate of return. MOLSS is studying the possibility of using the banks, including the Agricultural Bank of China, as a way to manage the funds.

¶13. (SBU) China wants to understand the U.S. experience in investment of pension funds, DDG Liu said. Mr. Lu Haiyuan, Director of the Department of Rural Social Insurance, MOLSS, has studied the U.S. experience, and written a book about how pensions in the United States are managed; many of his suggestions were included in China's 11th Five Year Plan. (Note: Individuals subsequently suggested for travel to the United States to study the U.S. system include MOLSS officials and asset management company personnel. End Note.)

¶14. (SBU) Comment: This savvy Deputy Director General's comments reflect his understanding of the numerous challenges he faces in making the rural pension system viable. Clearly, one of his high priorities is improving the rate of return on pension funds. MOLSS' Rural Social Security Office has for two years announced its interest in traveling to the United States to study how pension funds are managed, but travel has so far

not occurred. Laboff will again propose to MOLSS that the Embassy arrange a digital video conference to allow Washington agencies and interested others to address some of MOLSS' questions.

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